

The Wisconsin Inheritance Tax on Transfers Intended to Take Effect in Possession or Enjoyment at or After Death

Henry J. Marciniak

Follow this and additional works at: <http://scholarship.law.marquette.edu/mulr>



Part of the [Law Commons](#)

Repository Citation

Henry J. Marciniak, *The Wisconsin Inheritance Tax on Transfers Intended to Take Effect in Possession or Enjoyment at or After Death*, 40 Marq. L. Rev. 216 (1956).

Available at: <http://scholarship.law.marquette.edu/mulr/vol40/iss2/6>

This Article is brought to you for free and open access by the Journals at Marquette Law Scholarly Commons. It has been accepted for inclusion in Marquette Law Review by an authorized administrator of Marquette Law Scholarly Commons. For more information, please contact megan.obrien@marquette.edu.

THE WISCONSIN INHERITANCE TAX ON TRANSFERS INTENDED TO TAKE EFFECT IN POSSESSION OR ENJOYMENT AT OR AFTER DEATH

I. INTRODUCTION

The courts and legislatures have not been too successful in their attempts to dispel the somewhat common but erroneous impression that a state inheritance tax is imposed only on transfers by will or the intestate laws.¹ The contention is frequently raised on appeals from the imposition of the tax that it does not apply where the transferee takes by virtue of a contract or other inter vivos arrangement.² The constitutionality of the extension of the inheritance tax into the area of inter vivos transfers was decided at an early date.³ Historically, the possibility that inter vivos transfers might be used as a device to avoid an inheritance tax restricted only to transfers by will or under the intestate laws was first recognized by the Pennsylvania legislature in 1826.⁴ As a stopgap measure to prevent such tax avoidance, a clause was incorporated into the Inheritance Tax Act specifying that "transfers intended to take effect in possession or enjoyment at or after the death of the transferor" were subject to the inheritance tax. This general provision was adopted in Wisconsin in 1899⁵ and again in 1903,⁶ when the legislature borrowed its statute practically verbatim from New York. Since the enactment in 1933 of the Wisconsin Gift Tax Act,⁷ the question is not one of tax avoidance but whether the

¹ For example, Sec. 72.01(1) and (2) of the WISCONSIN STATUTES tax only transfers by will or intestate laws but Sec. 72.01(3) (a) taxes inter vivos gifts in contemplation of death and Sec. 72.01(3) (b) taxes inter vivos transfers intended to take effect at death. The earliest judicial comment is found in *State v. Pabst*, 139 Wis. 561, 121 N.W. 352 (1909): "The statute was not intended to restrict persons in their right to transfer property in all legitimate ways, but it clearly manifests a purpose to tax all transfers which are accomplished by will, the intestate laws and those made prior to death which can be classed as similar in nature and effect, because they accomplish a transfer of property under circumstances which impress on it characteristics of a devolution made at the time of the donor's death." (emphasis added) See also *Will of Allis*, 174 Wis. 527, 534, 184 N.W. 381, 383 (1921).

² This contention was sustained by the majority opinion in *Estate of Sweet*, 270 Wis. 256, 70 N.W.2d 646 (1955). See discussion by Justice Currie in his dissenting opinion. Contention was rejected in *Estate of Brackett*, 342 Mich. 195, 69 N.W.2d 164 (1955).

³ *Keeney v. New York*, 222 U.S. 525, 32 S.Ct. 105, 56 L.Ed. 299 (1912).

⁴ Leighton, *Origin of Phrase, 'Intended to Take Effect in Possession or Enjoyment At or After . . . Death'*, 56 YALE L. J. 176 (1946).

⁵ Chapter 355 of the Laws of 1899, subsection 3 of section 1. The language of the Wisconsin provision was modeled after the corresponding section of the New York Laws of 1892, Chapter 399, with amendments to 1895. It differed from the New York law in that it was limited to transfers of personal property in excess of ten thousand dollars. In 1902 the Wisconsin Supreme Court in its decision of *Black v. State*, 113 Wis. 205, 89 N.W. (1902) declared Chapter 355, as amended by chapter 245 of the Laws of 1901, unconstitutional.

⁶ Chapter 44 of the Laws of 1903 was passed to remedy the constitutional defect by making the inheritance tax applicable to all classifications of property.

⁷ Chapter 363 of the Laws of 1933, Wis. STATS. (1955), §72.75 et al.

inter vivos transfer is subject to either a gift tax or an inheritance tax. In view of the fact that Sec. 72.75(4)⁸ provides that no gift tax will be imposed upon the transfer of any property which is taxable under the inheritance tax law of this state, inter vivos transfers falling within the scope of the "transfer intended"⁹ provision, or within Sec. 72.01(3)(a) as a gift in contemplation of death, would not be subject to the gift tax.

The scope of Sec. 72.01(3)(b) taxing transfers intended to take effect at death is limited to transfers which are partially or wholly donative. There is some evidence in the Wisconsin decisions that it is not the purpose of this provision to subject to the inheritance tax strictly "arm's length" transactions.¹⁰ Prior to the 1949 amendment¹¹ this limitation was imposed by judicial decision¹² but now Sec. 72.01(3)(a) and (b) expressly exclude transfers for "an adequate and full consideration in money or money's worth." Under Sec. 72.76(1) a transfer, sale or exchange for less than "an adequate and full consideration in money or money's worth" is deemed a gift for gift tax purposes to the extent the clear market value exceeds the consideration received. The money equivalent limitation does not distinguish the transfer intended to take effect at death from a gift in contemplation of death or an inter vivos gift under Sec. 72.75. However, it is important to note that the gift tax is imposed on the excess of the clear market value over the consideration received while the inheritance tax appears to be measured by the entire clear market value of the property without an allowance for any consideration received.¹³

What primarily distinguishes the transfer intended to take effect at death from a gift in contemplation of death or a gift for gift tax purposes is that it is incomplete at the time it is made and that the death of the transferor is a factor in completing the devolution of the property to the transferee. Under Sec. 72.01(3)(a) the subjective element that the gift be motivated by an expectation of death is a

⁸ All section citations in the text of this paper refer to the WISCONSIN STATUTES (1955).

⁹ For the purpose of convenience the phrase, "transfer intended," shall be used as an abbreviation of "transfer intended to take effect in possession or enjoyment at or after the death of the grantor."

¹⁰ Estate of Miller, 239 Wis. 551, 554, 2 N.W.2d 256 (1942): "The character of the transaction excludes the possibility of the existence of a commercial dealing or of an exchange in which a valuable and adequate consideration, as that which is used in testing a transaction of this nature, has passed so as to bar the levying of the tax."

¹¹ Chapter 172 of the laws of 1949.

¹² Will of Koeffler, 218 Wis. 560, 260 N.W. 638 (1935).

¹³ WIS. STATS. (1955) §72.01(8) imposes the inheritance tax on the fair market value of the property and only upon the excess of the exemptions. Unlike the gift tax provision, this section makes no express allowance for any partial consideration that may have passed to the transferor.

prerequisite,¹⁴ and this motivation is presumed to exist if the transferor dies within two years after the date of the transfer.¹⁵ Such an intent is not required under the "transfer intended" clause.¹⁶ An inter vivos transfer to be subject to a gift tax must be complete in the sense that the transferor has retained no beneficial interest in the property or any power to revest such interest in himself.¹⁷ A completed inter vivos gift may be subject to an inheritance tax only if it is made in contemplation of death.¹⁸

The distinction between these three types of inter vivos transfers is best illustrated by a consideration of three different fact situations. The first situation is where A makes an absolute transfer of property to B without receiving any consideration. The transfer is complete for gift tax purposes if the transferor retains no beneficial interest or any power to revest such interest in himself. It does not come under the "transfer intended" clause because death is not a factor in completing the devolution of the property. If A dies within two years of the date of the transfer and if the presumption that the transfer was in contemplation of death is not overcome, B must pay an inheritance tax on the clear market value of the property at the time of death and B is given a credit for the amount of the gift tax paid.¹⁹ In the second situation A transfers the fee in the property to B without receiving any consideration but subject to a reservation of the beneficial interest for his lifetime. The transfer is not complete for gift tax purposes under Sec. 72.76(7) because the transferor has not divested himself of all the beneficial interest in the property, assuming that the property

¹⁴ *State v. Pabst*, 139 Wis. 561, 121 N.W. 352 (1909). *Will of Daniels*, 225 Wis. 502, 274 N.W. 435 (1937).

¹⁵ WIS. STATS. (1955) §72.01(3) (a).

¹⁶ *Estate of Schranck*, 202 Wis. 107, 230 N.W. 691 (1930).

¹⁷ WIS. STAT. (1955) §72.76(7): "A gift shall be complete for tax purposes when the donor has divested himself of all beneficial interest in the property transferred and has no power to revest any such interest in himself or his estate." This section apparently complements Sec. 72.01(3) (b), the "transfer intended" provision, which attempts to define what type of beneficial interest and what powers retained will subject the intervivos transfer to an inheritance tax at the death of the transferor, or in other words, specifies the criteria for an *incomplete* intervivos transfer subject to the inheritance tax.

¹⁸ A gift complete for tax purposes within the meaning of Sec. 72.76(7) may come under Sec. 72.01(3) (b). Where the donor does not divest himself of the power to designate the beneficiaries or any other power other than the power to revest the beneficial interest in himself or his estate, the gift would be complete for gift tax purposes, providing the retention of the power might not be considered, in effect, as the retention of the beneficial interest in the property. Despite the completeness of the transfer under Sec. 72.76(7), if the retained power comes under Sec. 72.01(3) (b), it is subject to an inheritance tax by virtue of Sec. 72.75(4). If the retained power does not come under Sec. 72.01(3) (b), it may still be taxed as a transfer in contemplation of death if it satisfies Sec. 72.01(3) (a). It appears that a transfer may be complete for gift tax purposes but incomplete for purposes of inheritance taxation under the "transfer intended" clause.

¹⁹ WIS. STAT. (1955) §72.75(4).

is considered a single indivisible unit.²⁰ Even if A dies within two years after the date of such a transfer, the incompleteness of the transfer should not prevent it from being taxed as a transfer in contemplation of death.²¹ But since the death of the transferor is necessary to complete the devolution of the property, it is taxable under the "transfer intended" clause. In the third situation A transfers absolutely without receiving any consideration the beneficial interest in the property to B for a period measured by A's life, and then, at the death of A the remainder in fee is to go to C. It is assumed that B is not closely related to A, because if such a relationship existed, a court might readily find that A in effect reserved the beneficial interest in the property for his lifetime.²² In view of the fact that the "transfer intended" clause requires either a reservation of a beneficial interest in the property or the retention of some power of control and that the gift tax provision requires a divestment of all the beneficial interest in the property and the divestment of any power to revest such interest, it appears that the legislature intended that the completeness of the transfer be the dividing line between transfers intended to take effect at death and transfers subject to a gift tax.²³ Once the transfer is complete in the lifetime of the transferor, his death is no longer a factor necessary to complete the devolution of the property from him.^{23a} The transfer to both B and C would, therefore, be subject to a gift tax.

By way of a brief summary, it can be stated that an inter vivos transfer, in trust or otherwise, will be subject to an inheritance tax at the death of the transferor under Sec. 72.01(3)(b) if the transfer is partially or entirely donative and if the transfer is incomplete in that the transferor has retained the beneficial interest in the property for his lifetime or some requisite power of control, which makes his death a factor in completing the devolution of the property from him to another.

²⁰ It is assumed that the property is one indivisible unit because if the property consisted of severable units, it would be possible to have a gift complete for gift tax purposes under Sec. 72.76(7) of the severable units equal to the difference between the total number of units and the units representing the beneficial interest retained by the transferor.

²¹ A transfer is deemed in contemplation of death within the meaning of Sec. 72.01(3)(a) if it is (1) by deed, grant, bargain, sale or gift, (2) made within 2 years prior to the death of the grantor, vendor or donor, of a material part of his estate, or in the nature of a final disposition or distribution thereof, and (3) without an adequate and full consideration in money or money's worth. Apparently, whether the transfer is complete within the meaning of Sec. 72.76(7) or Sec. 72.01(3)(b) is immaterial so long as the requirements of a transfer in contemplation are satisfied and the presumption is not rebutted.

²² *People v. Moses*, 363 Ill. 423, 2 N.E.2d 724 (1936), *In re Brockett's Estate*, 111 N.J. Eq. 183, 162 Atl. 150 (1932).

²³ *Supra*, note 18. A transfer is complete when the requirements of Sec. 72.76(7) and Sec. 72.01(3)(b) are met.

^{23a} See, however, footnote 80 *infra*.

It is the purpose of this paper to review the Wisconsin decisions in the light of the present statutory provision and other pertinent state court decisions in order to earmark the types of inter vivos transfers that may be taxed under the "transfer intended" clause.

II. INTER VIVOS TRANSFERS WHERE THE TRANSFEROR RETAINED A BENEFICIAL INTEREST IN THE PROPERTY FOR HIS LIFETIME

The Wisconsin court in its early decisions involving the "transfer intended" clause took the position that the retention by the transferor of the beneficial interest and the retention of a certain degree of control were two basic factors in determining the taxability of donative transfers under the clause.²⁴ The distinction between the retention of a beneficial interest and the degree of control was given additional emphasis in the 1949 legislative interpretation of the clause.²⁵ Sec. 72.01(3)(b) now expressly includes within the purview of the clause "any transfer where the transferor has retained for his life or for any period not ending before his death: 1) the possession or enjoyment of, or the right to the income, or to economic benefit from, the property, or 2) the right, either alone or in conjunction with any person, to alter, amend, revoke or terminate such transfer, or to designate the beneficiary who shall possess or enjoy the property, or the income, or economic benefit therefrom."

This distinction serves as a logical starting point in the analysis of the various cases. Thus, if the transferor retains no right of control over the property but retains the beneficial interest, the transfer is intended to take effect when the shifting of the beneficial interest occurs. Here the timing of the transfer becomes a crucial factor. In view of the express language of Sec. 72.01(3)(b) specifying "any period not ending before his death," whether a transfer involving a retention of the beneficial interest for a definite period of time comes within the clause depends on when the actual shift occurs. If it occurs at or after the death of the transferor, it is caught under the clause. If it occurs during the lifetime of the transferor, it is not within reach of the clause. However it may still be taxed as a gift in contemplation of death²⁶ or subjected to a gift tax.²⁷ The mere fact that the transfer creates a vested remainder during the lifetime of the transferor does not exclude it from the operation of the clause if there is a shifting of the beneficial interest at or after the death of the transferor.²⁸

²⁴ *Estate of Prang*, 201 Wis. 636, 639, 231 N.W. 271 (1930): "The test to be applied is whether donor reserved to himself any beneficial or economic interest, or any right thereafter to otherwise dispose such interest in the corpus of the trust for the benefit of himself or otherwise." This test was applied in *Estate of Waite*, 208 Wis. 307, 242 N.W. 173 (1932).

²⁵ *Supra*, note 11.

²⁶ WIS. STATS. (1955) §72.01(3) (a).

²⁷ WIS. STATS. (1955) §72.75.

²⁸ *Estate of Waite*, 208 Wis. 307, 242 N.W. 173, 174 (1932).

A. THE TRANSFER RETAINS THE POSSESSION AND ENJOYMENT OF THE PROPERTY FOR HIS LIFETIME

1. **Reservation of a Legal Life Estate.** The courts generally agree that where a transferor during his lifetime transfers by deed the remainder in fee and reserves to himself a life estate in the property, the remainderman will be subjected to an inheritance tax upon the death of the transferor under the "transfer intended" clause.²⁹ The law on this point was well settled when Wisconsin adopted its Inheritance Tax Act.³⁰ When a case involving a reservation of a legal life estate came up to the Supreme Court in 1930 for decision, this point was not even considered.³¹ The decedent in this case, approximately twelve years before his death and immediately before his second marriage, deeded the fee in all of his real estate to his three sons, subject to a reservation of a life estate in himself. The transfer was admitted to be in contemplation of marriage to prevent a second wife from acquiring dower rights in the property. The three remaindermen contended on appeal (1) that the "transfer intended" clause required an intention motivated by an expectation of death and (2) that if the transfer were subject to an inheritance tax, the tax should be imposed only on the value of the life estate at the time of the transfer in accordance with the provisions of Sec. 72.15(7), which restricts the tax to the increase of benefit to the remaindermen upon the termination of the life estate. The court ruled that it is not necessary that a transfer be motivated by considerations of death in order to be taxable under the "transfer intended" clause and that Sec. 72.15(7) is applicable only to a life estate based upon the life of some person other than the transferor. By virtue of Sec. 72.01(8) the remaindermen are taxed on the clear market value of the entire fee.

2. **A Reciprocal Trust.** An arrangement that closely parallels the reserved life estate situation is one type of the reciprocal trust. In this type of trust two settlors, usually close relatives, transfer legal title of property to a trustee in trust for themselves as beneficiaries.³² There is no immediate and present transfer of a beneficial interest to anyone else. Under the terms of the trust agreement the survivor takes the entire beneficial interest in the corpus of the trust created by the first to die. In effect, each settlor retains the beneficial interest in his own property for his lifetime, and the beneficial interest in one trust shifts when the first settlor dies.

A comparable arrangement was involved in the *Estate of Miller*.³³ In this case two sisters, owners of equal undivided interests in real

²⁹ See 139, 167 A.L.R. 1056, 443 (1947).

³⁰ Matter of Brandreth, 169 N.Y. 437, 62 N.E. 563 (1902).

³¹ Estate of Schranck, 202 Wis. 107, 230 N.W. 691 (1930).

³² In re Perry's Estate, 111 N.J. Eq. 176, 162 Atl. 146 (1932).

³³ Estate of Miller, 239 Wis. 551, 2 N.W.2d 256 (1942).

estate sold it, taking in payment a note secured by a trust mortgage. The note provided that each sister was to receive her proportionate share of the interest payments and that the principal payable to the trustee was to be paid to the survivor on the death of the other sister. The Wisconsin court did not hesitate to look behind the form of the arrangement to find that the transaction came within the "transfer intended" clause, being essentially a situation where the transferor reserves a life estate.

3. **Transferor Delivers Deed Absolute on its Face But Retains Possession and Enjoyment of the Property by an Extrinsic Agreement.** Analogous to an express reservation of a legal life estate is the arrangement where the transferor executes a deed absolute on its face but by virtue of an extrinsic agreement actually retains the possession and beneficial use of the property. If the form of the transaction is ignored, the transferor has in fact reserved for himself a life interest in the property. This type of an arrangement was involved in the *Estate of Odgen*.³⁴ Approximately three years and eight months before his death, the decedent deeded to his daughter by warranty deed certain real estate. It was understood between the father and the daughter that the father would retain the benefit of all the income from the property and pay all the operating expenses during his lifetime. The Wisconsin court found that the parol evidence rule was no obstacle to the admissibility of any oral or written extrinsic evidence to prove that the transferor had in fact retained the possession and enjoyment of the property and ruled that the arrangement was taxable under the "transfer intended" clause because the transferor had retained the beneficial interest in the property and the benefits did not actually shift until his death. The court, after having looked behind the form of this patent attempt at tax avoidance, suggests that "in order to escape the tax in this state the transfer must pass property from the transferor with all the attributes of ownership independently of his death."³⁵

How a transferor may intentionally attempt to conceal a retained beneficial interest is illustrated in numerous decisions in other states interpreting the "transfer intended" clause.³⁶ The shape and form of the device is limited only by the ingenuity of the transferor. A common device employed is to camouflage the inter vivos transfer by the use of two separate instruments, both of which appear to be complete on their face. However, when the two instruments are considered

³⁴ *Estate of Odgen*, 209 Wis. 162, 244 N.W. 571 (1932).

³⁵ This decision antedates the Gift Tax Act. Currently, the problem is not one of escaping taxation but whether the transfer is subject to either a gift tax or an inheritance tax.

³⁶ Rottschaefer, *Taxation of Transfers Intended to Take Effect in Possession or Enjoyment at Grantor's Death*, 26 IOWA L. REV. 514 (1941).

together, their combined effect is to give the transferor a beneficial interest for his lifetime. A typical example of such an arrangement is an absolute deed of conveyance fully executed and delivered to the beneficiaries but combined with a lease back to the grantor for a nominal consideration³⁷ or a bond³⁸ or other agreement which in effect gives the grantor the economic benefits from the property.³⁹ Other examples involve transfers to a straw man who transfers to a trustee to pay a fixed income to the original grantor for life⁴⁰ or an absolute transfer in trust subject to the settlor's present and future liabilities.⁴¹ These cases indicate a general willingness on the part of the courts to look behind the literal provisions of an agreement and to emphasize the substance rather than the form of the agreement.

4. U.S. Government Savings Bonds. The acquisition of U.S. Government Savings Bonds poses a problem under the "transfer intended" clause which in recent years various state courts have attempted to solve with somewhat conflicting results.⁴² In the majority of bond purchases it is the actual purchaser who advances the entire consideration and becomes the registered owner with the right to designate another party as a co-owner or the person to whom the bond will be payable on the purchaser's death. As a general rule, the registered owner, having paid for the bond, retains possession of the bond and under the Federal Regulations has the right to cash the bond in at any time during his life without consent of the co-owner or other beneficiary.⁴³ In effect, the registered owner retains the beneficial interest in the bond for his lifetime and on his death the beneficial interest shifts to another.

To maintain a position consistent with these general principles some courts have held that where the decedent-purchaser of the bonds retains possession of them until his death, the transfer of his right to the payment is taxed under the "transfer intended" clause.⁴⁴ Where the purchaser survives the co-owner or other beneficiary, the transfer

³⁷ *Moor v. Bugbee*, 3 N.J. Misc. 435, 128 Atl. 679 (1925), affirmed in 102 N.J.L. 720, 135 Atl. 919 (1927).

³⁸ *In re Cornell's Estate*, 170 N.Y. 423, 63 N.E. 445 (1902).

³⁹ *Brandreth's Estate*, 169 N.Y. 437, 62 N.E. 563 (1902).

⁴⁰ *In re Miller's Estate*, 236 N.Y. 290, 140 N.E. 701 (1923).

⁴¹ *In re Dubois's Appeal*, 121 Pa. 268, 15 Atl. 641 (1888).

⁴² 39 A.L.R.2d 690 (1955).

⁴³ CODE OF FEDERAL REGULATIONS, Title 31, §315.45 and 315.46.

⁴⁴ Series E co-ownership bonds were held to be taxable under the "transfer intended" clause: *Rummel's Estate* 74 S.D. 131, 49 N.W.2d 380 (1951), *Brown's Estate*, 122 Mont. 451, 206 P.2d 816 (1949). The Montana Statute was amended after this decision to subject one half of the value of the bond to the tax instead of the entire value.

Series E payable-on-death bonds held to be taxable as a transfer intended to take effect at death: *Mitchell v. Carson*, 186 Tenn. 228, 209 S.W.2d 20 (1948). The Michigan court refuses to tax either type of bond. See *DeWater's Estate*, 338 Mich. 457, 61 N.W.2d 779 (1953).

has been held not taxable.⁴⁵ No beneficial interest shifts to the purchaser at the death of the other party. Other courts have applied statutes taxing jointly owned property to U.S. Government bonds.⁴⁶

The Wisconsin court has not ruled upon the question of the taxability of either type of bond. The bonds might be taxed under Sec. 72.01(6) as jointly owned property and a tax might be imposed on one half of the value of the bond in the same manner that a joint bank account is taxed. The analogy between the government bond and the joint bank account is very tenuous. In the case of the latter, either joint owner can sever the right of survivorship as to funds withdrawn. The co-owners of government bonds have no comparable rights. The purchaser of the bond is the absolute owner during his lifetime so long as he retains dominion and control over the bond and if he cashes it in during his lifetime, the co-owner is entitled to nothing. The analogy completely breaks down when it is applied to the bond payable on death.

Taxing the government bonds as jointly held property also creates a difficult tax enforcement problem where the purchaser of the bond is the survivor. Generally, the purchaser retains possession of the bonds, and when the other party dies, his personal representative has no way of ascertaining the prior rights of the decedent. It cannot be expected that the purchaser will volunteer any payment of the inheritance tax when he has the right to obtain payment of the bonds during his lifetime and can exercise this right after the death of the other party.

The more realistic approach to the problem is to view it as a transfer intended to take effect at death. The purchaser by designating a co-owner or other beneficiary on the face of the bond creates a right in such person to obtain payment at or after the death of the purchaser. Certainly, under the Federal Regulations the purchaser has retained for his lifetime the beneficial interest in the bonds, that is, the right to convert the bonds into cash.⁴⁷ Where the bond is made payable on death to some designated beneficiary, the beneficiary interest retained by the purchaser shifts to the beneficiary at the death of the purchaser. Where the bond is made out in co-ownership form, the purchaser retains the beneficial interest in the bonds so long as he retains dominion and control over the bonds in as much as the Federal Regulations allow the designated co-owner in possession of the bonds to obtain payment without the consent of the purchasing co-owner.⁴⁸ A surrender of dominion and control over the bonds to the designated co-

⁴⁵ *Heinlein's Estate*, 30 *ERIE Co. L. J.* 27 (1947).

⁴⁶ *McGary's Estate*, 355 Pa. 232, 49 A.2d 350 (1946). *Hallett v. Bailey*, 143 Me. 1, 54 A.2d 533 (1947).

⁴⁷ *Supra*, note 43.

⁴⁸ *Supra*, note 43.

owner constitutes a completed inter vivos gift.⁴⁹ The retention of possession of the bonds by the purchasing co-owner for his lifetime causes the shift of the beneficial interest to occur at his death and, therefore, comes within the reach of the "transfer intended" clause.⁵⁰ In the event that the purchasing co-owner survives the designated co-owner, the survivor is not taxed under the clause because the beneficial interest does not shift at the death of the designated co-owner.⁵¹

5. Contracts Concerning Transfers of Business Interests at Death. A transferor may retain the beneficial interest in property for his lifetime and cause a shift in this beneficial interest to occur at or after his death pursuant to the terms of a contract.⁵² Partnership agreements and stock option agreements between the principal stockholders in a closely held corporation frequently provide for the transfer to the survivors of the decedent's interest.⁵³

A contract involving a performance timed to occur at the death of one of the parties should be distinguished from a contract to execute mutual provisions in a will. The latter type of contract was involved in the *Will of Jones* where two principal corporate stockholders entered into a contract that each would provide in his will that the other should have an option to purchase a specific number of shares in the corporation at twenty-five percent below the appraised value of the shares.⁵⁴ The benefit to a surviving stockholder under such an agreement passes by virtue of the decedent's will and is taxed as a transfer by will under Sec. 72.01(1).

Where the provision in a partnership agreement provides that upon the death of a partner his share in the assets of the firm should become the property of the survivor without any payment to his estate, courts have held such a devolution of property taxable under the "transfer intended" clause.⁵⁵ The provisions in a partnership agreement stipulating that for the purpose of evaluating a decedent's partnership interest, the good will and partnership name shall have zero valuations have likewise been caught under the clause.⁵⁶ The view that the analogous stock option agreements fall within the clause finds support in both the state and federal decisions.⁵⁷

The Wisconsin attorney confronted with the problem of drafting

⁴⁹ *Littlejohn v. County Judge, Pembina County*, 58 N.W.2d 278 (N. Dak., 1953).

⁵⁰ *Ibid.*

⁵¹ *Heinlein's Estate*, 30 ERIE Co. L. J. 27 (1947).

⁵² Justice Black supported the view that such contracts create transfers intended to take effect at death in *Commissioner v. Church* 335 U.S. 632, 69 S.Ct. 322, 93 L.Ed. 291 (1947).

⁵³ Comment, *Options and Sale Contracts in Taxation*, 46 YALE L. J. 272.

⁵⁴ *Will of Jones*, 206 Wis. 482, 240 N.W. 186 (1932).

⁵⁵ *Minoff v. Margetts*, 14, N.J. Super. 30, 81 A.2d 369 (1951).

⁵⁶ *Deitz's Estate*, 105 N.J. Eq. 671, 149 Atl. 257 (1930). *Halle's Estate*, 103 Misc. 661, 170 N.Y. Supp. 898 (1918).

⁵⁷ *Supra*, note 52. 157 A.L.R. 973 (1945).

a buy and sell provision or a stock option agreement to provide continuity of management and control of the business in the event of the death of a partner or principal stockholder should not lose sight of the inheritance tax consequences. Under the rule of the *Will of Jones* the agreement should not require the parties to execute provisions in their wills to transfer their interest to the survivor upon death. Even if a full and adequate consideration in money or money's worth is paid to the estate, Sec. 72.01(1) does not exclude such transfers. Transfers satisfying the money equivalent requirement are excluded from taxation under the "transfer intended" clause.⁵⁸ An agreement to purchase at some fractional part of the appraised value, such as was contained in the *Will of Jones*, fails to satisfy the money equivalent requirement and is subject to the risk of being taxed on its entire clear market value under the "transfer intended" clause. Likewise, provisions assigning a zero evaluation to good will and the firm name should be avoided.⁵⁹

B. THE TRANSFEROR RETAINS THE RIGHT TO THE INCOME OR ECONOMIC BENEFIT FROM THE PROPERTY FOR HIS LIFETIME

It is well settled law that any inter vivos transfer under the terms of which the transferor retains a right to the income from the property is taxable under the "transfer intended" clause.⁶⁰ Sec. 72.01(3)-(b) expressly includes transfers where the transferor retains the right to the income from the property for his life or for any period not ending before his death. The type of fact situation now to be considered differs from those discussed in sub-part A in that the transferor has divested himself of the possession of the property. It should be noted that these particular classifications are not mutually exclusive. Where a transferor parts with the bare legal title and retains possession and the income from the property for his lifetime, a fact situation that overlaps both classifications is posed. Regardless of what the particular classification may be, under the "retention of beneficial interest" test, it comes within the scope of the "transfer intended" clause.

In the *Estate of Waite*⁶¹ the Wisconsin court was called upon to decide whether an irrevocable trust agreement entered into by the decedent approximately eleven years before his death was taxable under the clause. The decedent transferred to a trustee shares of stock in trust to pay to himself an annual income during his life and upon

⁵⁸ WIS. STATS. (1955) §72.01(3) (b). [*Estate of Banta*, 273 Wis. 328, 77 N.W.2d 730 (1956) held the consideration must be adequate at time of transferor's death and not merely at time agreement was made. Ed.]

⁵⁹ *Supra*, note 56.

⁶⁰ 85 C.J.S., TAXATION §1147(3) (d), see cases cited at page 939.

⁶¹ 208 Wis. 307, 242 N.W. 173 (1932).

his death half of the corpus was to go to his son and the other half was to be administered for the benefit of the grandchildren. The principal contention of the beneficiaries on appeal was that the remainder was vested at the time of the trust agreement and therefore nothing passed from the transferor at the time of his death. The court properly declined to apply the technical property concepts of vesting and held the case to be within the rule set forth in the *Will of Prange*⁶² that the retention of a beneficial interest or the right to dispose of such interest in the corpus of the trust for the benefit of himself or otherwise is a controlling factor in determining taxability under the clause.

A long line of decisions in the state courts have held that an agreement by the transferee to pay income to the transferor for life is not taxable if the actual property transferred is not bound to produce the money to be paid.⁶³ The Wisconsin court joined the ranks in its decision of the *Estate of Hamilton*.⁶⁴ The decedent in this case at the age of sixty-four purchased from various religious societies bonds payable to his order in fixed periodic payments for the duration of his life. It was conceded that the purchase of the bonds was partly donative in that the decedent could have purchased annuity policies for the same amount of money from insurance companies and would have realized a much higher return. The overpayment by the purchaser presented the court with no problem because the court correctly held that there was an absolute transfer at the time of the purchase. The excess of the price paid over the clear market value of the annuity constitutes a completed inter vivos gift. The transaction does not come within the scope of the "transfer intended" clause because there is no shifting of a beneficial interest in the property actually transferred at the death of the transferor, the shift having occurred in his lifetime.

Transferring the right to the income or the power to determine the amount of the income to a close relative of the transferor may not place the transfer outside the scope of the clause if the court finds that the transferor has actually retained the economic benefit from the property.⁶⁵ In an Illinois case⁶⁶ the power to determine the amount of income to be paid out of the trust was vested in a trustee who was a close relative of the settlor. The court found that this in effect amounted to the retention of the economic benefit from the property for the transferor's life and held the transfer taxable at his death under the "transfer intended" clause.

⁶² 201 Wis. 636, 231 N.W. 271 (1930).

⁶³ 85 C.J.S., *Taxation* §1147(3) (c). See cases cited in footnote 10 at page 934.

⁶⁴ 217 Wis. 491, 259 N.W. 433 (1935).

⁶⁵ *Supra*, note 22. *Koch v. McCutcheon*, 111 N.J. L. 154, 167 Atl. 752 (1933).

⁶⁶ *People v. Moses*, 363 Ill. 423, 2 N.E.2d 724 (1936).

Not only may the retention of a present economic benefit result in taxability under the clause but the retention of a possible economic benefit in the future from the property may also have the same effect. How a transferor may inadvertently retain such a benefit was forcefully illustrated in the *Spiegel* case,⁶⁷ where a reversionary interest was retained by the settlor because the trust agreement failed to provide for a gift over in the event that the settlor survived the beneficiaries. Whether the existence of this reversionary interest in the transferor is sufficient in itself to bring the transfer within the reach of the "transfer intended" clause is a question on which there is no Wisconsin case and in other jurisdictions the cases are in conflict.⁶⁸ These cases illustrate the necessity of providing a gift over in a trust agreement to prevent a reversion from arising out of the possibility that the settlor may survive his beneficiaries even though the contingency is extremely improbable and may in fact never occur.

III. INTER VIVOS TRANSFERS WHERE THE TRANSFEROR RETAINS THE RIGHT, EITHER ALONE OR IN CONJUNCTION WITH ANY PERSON, TO ALTER, AMEND, REVOKE OR TERMINATE SUCH TRANSFER, OR TO DESIGNATE THE BENEFICIARY

The Wisconsin legislature in passing the 1949 amendments to the "transfer intended" provision⁶⁹ and the complementary gift tax⁷⁰ provision apparently intended to set up two broad tests for determining taxability of an inter vivos transfer. Various aspects of the "retention of beneficial interest" test were discussed in Part II of this paper. The second test or the "retention of control" test shall now be considered. Prior to the 1949 amendments the Wisconsin court in construing and applying the "transfer intended" clause recognized that the retention by the transferor of a right to dispose of the beneficial interest in the property might be equivalent to the actual retention of a beneficial interest in the transferor for his lifetime.⁷¹ Under this

⁶⁷ *Spiegel v. Commissioner*, 335 U.S. 701, 69 S.Ct. 301, 93 L.Ed. 330 (1949). This decision was instrumental in bringing about the Technical Changes Act of 1949 which redefined the "transfer intended" clause for federal estate tax purposes.

⁶⁸ See cases collected in 85 C.J.S., TAXATION, §1149(3)(d), footnote 39 at page 937-8. *People v. McCormick*, 327 Ill. 547, 158 N.E. 861 (1927), *Estate of Dunlap*, 205 App.Div. 125, 199 N.Y. Supp. 147 (1923), *Boston Safe Deposit and Trust Co. v. Commissioner*, 267 Mass. 240, 166 N.E. 729 (1929).

⁶⁹ *Supra*, note 11.

⁷⁰ *Supra*, note 17.

⁷¹ In the *Estate of Prange*, 201 Wis. 636, 231 N.W. 271 (1930), the court dealt with a trust agreement under the terms of which the settlor retained the right to vote the stock in a closely held corporation. About two and a half years before his death the decedent transferred the controlling shares of stock to a corporate trustee to be held in trust for a period of thirty years with the power to distribute the income annually during the thirty year period and at the termination to distribute the corpus to the five children of the settlor or their issue. The right to vote the controlling shares of stock was to vest in the beneficiaries of the trust at the death of the settlor. The court held that the

judicial test it was required that there be an increase in value of the property transferred when the right to dispose of the beneficial interest was terminated by the transferor's death. Under the statutory test prescribed by the 1949 amendment, it appears that it is no longer necessary that there be an increase in value of the property in the hands of the transferee as a result of the termination of the right of control at the death of the transferor.⁷²

If the "retention of control" test is satisfied, the transfer comes under the "transfer intended" clause irrespective of when the shift of the beneficial interest occurs, unless the transferor's right of control terminates within his lifetime. Where the right of control terminates within the transferor's lifetime, the controlling factor becomes the time at which the shifting of the beneficial interest occurs. In the run-of-the-mill fact situation the rights of control retained are not qualified by any time limitation. The death of the transferor is a factor in the devolution of the property in such cases because the right or the "string attached" is cut off by his death. The critical point in such cases is not the timing element, but the extent or the degree of control over the property retained by the transferor. Whenever the courts are confronted with questions of degree, the decisions are invariably marked by sharp conflicts.⁷³ In order to resolve to some extent the conflict existing among the courts, the 1949 amendment to Sec. 72.01(3) expressly included transfers where the control retained consists of the right, either alone or in conjunction with any person, to alter, amend, revoke or terminate the transfer, or to designate the beneficiary of the transfer.

1. *Inter Vivos Trusts.* The "transfer intended" clause has been effectively used by the courts in attacking the inter vivos trust, which is well adapted to schemes of tax avoidance.⁷⁴ Because of this possibility the clause is expressly applicable to transfers "in trust or other-

mere reservation of the right to vote the controlling stock did not amount to the retention of an economic benefit that would pass to the beneficiaries at the death of the transferor.

⁷² WIS. STATS. (1955) §72.01(3) (b).

⁷³ See annotation in 155 A.L.R. 850 (1945). The mere right to revoke trust does not render an estate subject to tax. *Masury's Estate*, 28 App.Div. 580, 51 N.Y. Supp. 331 (1898), *aff'd* 159 N.Y. 532, 53 N.E. 1127 (1899). *Contra*, *Cochran v. McLaughlin*, 129 Conn. 176, 27 A.2d 120 (1942). Where power is reserved not to settlor alone but is to be exercised by him in conjunction with another person, it was held that if interest of the other person was sufficiently adverse, the transfer was not subject to the succession tax because "any person" in the New York statute means any person not having a substantial adverse interest. See in matter of *Stewart's Estate*, 138 Misc. 866, 248 N.Y. Supp. (1931), *aff'd* 235 App.Div. 772, 255 N.Y. Supp. 970 (1932).

⁷⁴ The decided cases under the "transfer intended" clause involve predominantly inter vivos trusts. How the various courts have used the clause in attacking the inter vivos trust with conflicting results is set forth in an interesting comment in 79 UNIV. PA. L. REV. 185 (1930).

wise."⁷⁵ While the courts will agree that where a settlor retains a beneficial interest in the form of income for his lifetime such a transfer falls within the scope of the clause,⁷⁶ the courts are not as willing to agree on the issue of taxability where the settlor parts with the economic benefits of the property but retains the right to control the disposition of these benefits.⁷⁷

A failure on the part of some courts to distinguish between the three basic trust arrangements that come within the purview of the clause has resulted in a maze of decisions.⁷⁸ These three distinguishable basic arrangements are:

- (1) Under the terms of the trust agreement the settlor retains all or part of the economic benefits from the property for his lifetime with or without any rights of control over the property,
- (2) Under the terms of the trust agreement the settlor parts with all the economic benefits from the property but retains the requisite degrees of control over the property, and
- (3) Under the terms of the trust agreement the settlor retains neither any economic benefits from the property nor any control but his death is a factor in the devolution of the corpus of the trust.

Arrangement number (1) is nothing more than the equivalent of a reservation of a life estate with a remainder over to certain beneficiaries. The presence or absence of any right of control does not affect the taxability under the "transfer intended" clause.⁷⁹ Arrangement (2) involves the "retention of control" test. What rights retained place the transfer within the purview of the clause are specified in part in Sec. 72.01(3)(b). Arrangement number (3) is the equivalent of the transfer of a life estate measured by the life of the transferor with a remainder over to other beneficiaries. This situation arises when the trust agreement provides for the termination of the trust at the death of the settlor and for a distribution of the corpus at such time.⁸⁰ The fact that the settlor has not retained any control or

⁷⁵ WIS. STATS. (1955) §72.01.

⁷⁶ *Supra*, note 74.

⁷⁷ Estate of Bullen, 143 Wis. 512, 128 N.W. 109 (1910).

⁷⁸ Topping v. McLaughlin, 125 Conn. 456, 6 A.2d 343 (1939), *contra*, People v. Armiger, 372 Ill. 415, 24 N.E.2d 355 (1939). Other cases are extensively annotated in 155 A.L.R. 850 (1945).

⁷⁹ If the "retention of beneficial interest" test under Sec. 72.01(3)(b) is satisfied, the transfer is caught under the "transfer intended" clause and is taxable. No further analysis under the "retention of control" test is necessary.

⁸⁰ Fabian v. Walsh, 134 Conn. 456, 58 A.2d 384 (1948). The settlor reserved no interest or control in the trust but it was to terminate upon the decease of the survivor of the settlor and her husband and upon termination of the trust the corpus of the trust was to be distributed to a daughter. The husband predeceased the settlor. The court held the transfer taxable under the "transfer intended" clause because the death of the settlor was a necessary factor to effectuate the transfer to the daughter. See Matter of Cruger, 54 App.Div. 403, 66 N.Y.Supp. 636 (1900), *aff'd* 166 N.Y. 602, 59 N.E. 1121 (1901), where the

beneficial interest in the property should exclude it from taxability under the clause.⁸¹

2. **Death Benefits Under Profit Sharing and Pension Trust Plans.** In recent years a number of the state courts have been confronted with the problem of determining whether the death benefits under federal retirement system, private profit-sharing and pension trust plans, and individual annuity contracts are taxable under the "transfer intended" clause. These decisions are characterized by their sharp conflicts.⁸²

The Wisconsin Supreme Court in a recent 4-3 decision⁸³ ruled that the death benefits payable to a widow under the Federal Civil Service Retirement Act⁸⁴ were not taxable under the "transfer intended" clause. Under the federal retirement plan the beneficiaries are prescribed by law and the employee has no right to change the beneficiary. Both the government and the employee contributed to the plan. The widow under the plan was entitled to an annuity of \$185.00 per month for life, the annuity having a present value of 18,907.96 based on the life expectancy of the widow.

The majority opinion relied upon several New York decisions involving life insurance contracts payable to specific beneficiaries and holding that such insurance payments upon death are immune to the succession tax because they do not pass into the estate of the insured and are not therefore subject to the Inheritance Tax Act. It also cited with approval the reason given in the New York cases that insurance benefits payable to the dependents of the insured are charged with a

fact that the settlor's death determined the time of distribution was held to render the transfer taxable when the remainderman was not the beneficiary of the income during the settlor's lifetime. In view of the Wisconsin rule of statutory construction that where a statute has received a judicial construction in another state and such statute is then adopted in Wisconsin, it is taken with the construction which has been so given to it. *Estate of Sweet*, 270 Wis. 256, 70 N.W.2d 646 (1955), it may be contended that the above New York decision is a part of Wisconsin law.

This problem may also have been involved in *Will of Fehlhaber*, 272 Wis. 327, 75 N.W.2d 444 (1956), when the deceased delivered prior to her death promissory notes and U.S. Government bonds to her son and instructed him to share them equally with his sister at the time of her death. The decision does not disclose who retained the beneficial interest in the property from the time of delivery to the time of her death. The court held without discussion that the transfer came within the purview of Sec. 72.01(3)(b).

⁸¹ This question has not been judicially answered in Wisconsin. In view of the dual test provided in Sec. 72.01(3)(b), unless either one of these tests are met, the transfer should be excluded.

⁸² *In re Dorsey's Estate*, 336 Pa. 557, 79 A.2d 259 (1951), *In re Daniels*, 93 Ohio App. 123, 112 N.E.2d 56 (1953), *Garos v. State Tax Commission*, 109 A.2d 844 (1954), *Borchard v. Connelly*, 140 Conn. 491, 101 A.2d 497 (1953).

⁸³ *Estate of Sweet*, 270 Wis. 256, 70 N.W. 2d 646 (1955).

⁸⁴ After the *Sweet* case was handed down, the Wisconsin legislature enacted Chapter 589, Laws of 1955 creating Sec. 72.04(6) which now exempts from the inheritance tax death benefits under the various state civil service pension funds.

public interest and unless the legislature clearly expresses an intention to tax such benefits the court would not do so as a matter of policy. In the dissenting opinion Justice Currie points out that the requirement that some interest pass under the laws of inheritance was expressly rejected in an earlier Wisconsin decision and is inconsistent with the express language of Sec. 72.01(3)(b). The dissent also indicates that the absence of any right in the decedent during his life to name or change the beneficiary is not a decisive factor where the decedent retained a beneficial interest in the pension fund during his lifetime and where this beneficial interest shifts to a beneficiary specified by law.⁸⁵ The beneficial interest which the decedent retained for his lifetime was in the nature of an annuity payable to him upon retirement, the amount of which was determined by his own and the government's contributions to the fund. His death is a factor in the devolution of this interest from him to the specified beneficiary. The position taken by the dissenting justices appears to be more consistent with the principles evolved in the earlier Wisconsin cases.

3. Savings and Loan Association and State Bank Trust Accounts. A recent California decision⁸⁶ highlights another current problem concerning the taxability under the "transfer intended" clause of trust accounts in a savings and loan association. In this case the decedent deposited a fund in trust for his adult son. The court, in holding the fund taxable had absolute control of the trust account.

Trust accounts, similar to the one involved in the California decision, are authorized under Sec. 215.18 and 221.44 for Wisconsin savings and loan associations and state banks. These sections provide that in the absence of notice of the existence and terms of any valid trust, the deposit may be paid to the designated beneficiary in the event of the death of the trustee.

Under Wisconsin law the trustee has the absolute control over the trust account during his life. The beneficiary has no right to the account until the death of the trustee. Thus, the trustee who had deposited the fund retains the beneficial interest in the fund for his lifetime, and the beneficiary has no right to the possession and enjoyment of the fund until the death of the trustee. The payment of the account to the beneficiary after the death of the trustee, therefore, should be taxable under the "transfer intended" clause.

IV. AN ADEQUATE AND FULL CONSIDERATION IN MONEY OR MONEY'S WORTH — THE MONEY EQUIVALENT

It was not until 1949⁸⁷ that there was any statutory provision in

⁸⁵ *Supra*, note 77.

⁸⁶ *Estate of Goldfader*, 280 P.2d 799 (1955).

⁸⁷ Chapter 172 of the Laws of 1949.

Wisconsin excepting from taxation under the clause transfers for an adequate and full consideration in money or money's worth. Prior to this time such exception was granted by judicial decision⁸⁸ on the ground that where the transferor has received consideration for the property transferred, no interest passes by inheritance. The money equivalent requirement has been a prolific source of litigation in the federal courts and in some of the states.⁸⁹ In the federal courts the decisions have run the gamut of all the technical niceties of the common law concepts of consideration. The relinquishment of certain rights may be sufficient if the money equivalent requirement is satisfied. The relinquishment of marital rights is not generally considered a money equivalent. The Wisconsin Supreme Court in the *Will of Koeffler*⁹⁰ held in 1935 that a transfer of property at the death of the transferor pursuant to an ante-nuptial agreement was for an adequate consideration. The court intimated that "if our statute contained a provision to the effect that all property of the decedent, except such as might be due upon a contract consideration for money or money's worth, was subject to taxation, we should probably be obliged to reach a different result as the courts of Massachusetts and New York have done." In view of the fact that the Wisconsin statute now contains the money equivalent limitation and that by statutory amendment in 1953, the words "the intestate laws of this state" include rights acquired by contract in lieu of dower, transfers at death pursuant to an ante-nuptial agreement would now be subject to inheritance taxation under Sec. 72.01 (3)(b) and 72.01(1).

The decisive point under the money equivalent limitation appears to be whether or not the payment made to the transferor for the property equals the economic value of the property. There have been no decisions in Wisconsin construing the money equivalent limitation, but the corresponding Massachusetts statute is construed to require that the consideration passing from the beneficiary be at least equal in value to the property received.⁹¹ The burden of proof in such a case is on the party affirmatively asserting that the consideration is in money or money's worth. However, if the party proves only a partial consideration, there is no exemption provided for the partial amount.

V. CONCLUSION

An understanding of the full scope of the "transfer intended" clause becomes important to the attorney engaged in estate planning and to the attorney probating an estate. In view of Sec. 72.75(4)

⁸⁸ *Will of Koeffler*, 218 Wis. 560, 260 N.W. 638 (1935).

⁸⁹ 157 A.L.R. 964 (1945).

⁹⁰ 218 Wis. 560, 260 N.W. 638 (1935).

⁹¹ *State Street Trust Co. v. Stevens*, 209 Mass. 373, 95 N.E. 851 (1911).

which provides that no gift tax will be imposed upon the transfer of any property which is taxable under the inheritance tax law of this state, inter vivos gifts falling within the scope of the "transfer intended" clause are not subject to the Wisconsin gift tax but the payment of a gift tax cannot be considered complete protection against the later imposition of the inheritance tax. The 1953 amendment to Sec. 312.01 has provided the public administrator with a tool that may aid him in the enforcement of the "transfer intended" clause. The section now expressly imposes a duty upon the personal representative to file in his inventory for tax purposes all gifts taking effect at death which come to his possession or knowledge. If the personal representative petitions the court for instructions or if he goes ahead and includes a questionable transfer in the estate inventory, the public administrator and the interested donee are afforded an opportunity to contest the issue of taxability at the outset of the administration.

HENRY J. MARCINIAK